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## Small Countries: Are They Interested in FDI by TNCs?

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### Abstract

The so-called “rules” of international investment can be the model of interaction between small home-countries and TNCs<sup>2</sup>. In our opinion these rules might be considered as an attempt of construction of interaction model between participators of world investment process – exporters (TNCs) and importers (home-countries). That model gives an opportunity to take into account the interests of both sides.

**Key words:** FDI TNC; Small home-countries; “Rules” of international investment

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**The main hypothesis:** If the small home-countries are interested in FDI by TNCs, they should change there investment legislation in a direction to international investment’s rules.

### 1. “RULES” OF INTERNATIONAL INVESTMENT AS A MEANING OF BALANCING THE PARTICIPANT’S INTERESTS

Let’s call them and try to prove that each of these 4 rules is really an attempt to find the point of balance and so

to create a model where neither exporter country nor importer country would have an advantage in compare with another.

However this empiric check postulates that this is only an attempt and it is too early to speak about real both-beneficial interaction.

- Fair and equitable treatment or preferable nations.

There is need to pay attention for two moments here which include the next rule:

- ◊ all foreign investors should have an equal conditions;

◊ There shouldn’t be any difference between foreign and national investors. In fact the speech is about the opportunity of profit repatriation, transfer of salary and other pay-ments. However the foreign investors could work in equal as well as in better and worse conditions.

- Right of entry says that that TNC could make a foundation of office on the territory of any sovereign state and there is no need in special permission from authorities of home-country. It is understood that in this point of rule the only interests of foreign investors are in account. However in fact it isn’t always done by a reason of non-conformity with a national legislation power or national security threat. To take in account and satisfy the interests of home-country this rule is added with a position based on the legal norm: permitted everything which is not for-bidden. On practice it is realized in a manner that authorities of home-country publish the total number of territories and branches where the investment couldn’t be made. For example the Mexican constitution forbids the foreign investment in the branch of oil debit. Brazil restricts the foreign investment in industry of computers and telecommunications. The authorities of home-country could stimulate the attraction of foreign investment in definite regions of a country by creating a tax harbors or providing other privileges.

- Contract termination – The right of a home-country unilaterally to expropriate (to nationalize) the property of the foreign investor (branch of the multinational

corporation) under condition of non-observance of the current legislation. Many countries used this method. Heads of some of the African countries also did not hide, that development of local economy has begun after nationalization of the foreign enterprises. In 50th years the petroleum industry of Kuwait has been nationalized. In 60 - India has confiscated the enterprises of Coca-cola. In the beginning of 70th years in Chile the enterprises on extraction of copper have been nationalized. In 1979 the government of Nigeria has nationalized activities of the British oil company.

To protect interests of the second party of the contract-foreign investors, the certain accepted conditions of indemnification payment should be:

◊ Normal which means a fair payment of industrial market price. However there are some doubts over an opportunity of realization of this rule. What does the fair industrial market price mean? We shall use the same methodological approach so we consider this rule as an opportunity to take into account interests of both sides - participants of process. Let's start from importer and suppose that currency of his country is not a free convertible which is almost every time. When TNC buys a plant on a territory of home-country (with a worse GDP volume) its price is much more less than the price for the same plant in TNC's country<sup>3</sup>. Could it consider as a fair thing in relation to the importer state?! Probably hardly. Let's take another participant of process – exporter. The easily convertible currency is spent when an exporter buys a plant. Let's imagine that a sum of money is invested in easily convertible currency. Because in a majority of countries the mono-currency system is used this sum is converted into a national currency. Let it be the country X and the rate of its currency to the currency of Y country is 5 to 1. If the crisis happens the currency rate is falling. As it happened in Russia the currency level failed down in 6 times. What is going to be a fair market price of plant in that case and what currency rate must be used!? If it is 5 to 1 it is impossible for importer country. If it is 30 to 1 it is impossible for exporter country. Therefore this rule is not stable and needs the serious add-work to do.

◊ Effective. It means that a payment must be interacted in acceptable for foreign investor currency according to the market exchange rate on a day of a transfer.

◊ Fast. It means that the indemnification payment shouldn't have a not proved delay or there should be paid an additional percent over delayed sum of indemnification payment.

• Dispute of Settlement. Dispute is resolved by the court of home-country on the base of national legislation or impartial and independent arbitration on the base of international convention of investment dispute settlement whose members are people from approximately 120 countries and what is important they do the court said them to do.

For disputes of settlement several international conventions are acting. Exactly the mentioned above Washington convention "About the order of settlement of investment disputes" between the states and foreign investors and Seoul convention of 1985 which came into force in 1988. Russia ratified these conventions in 1992.

We were following a several criteria while we were choosing the countries for empiric check on their practical realization. First of all the chosen countries for analysis are the small opened economies. Secondary the similarity with Russia according to the parameters of investment climate was taken into account. The most important of them are the political media and legislation. That is why they became a base for analysis of chosen countries: Jordanian<sup>4</sup>, Syria<sup>5</sup>, Oman<sup>6</sup>, and Israel<sup>7</sup>. Thirdly, specialty of export resource orientation of Russia was taken into account: because of non-favorable influence of oil profit on the development of other branches of economy, Venezuela, Norway as a seller of oil and not a member of OPEC were chosen. Finally the investment experience of Russia of being a member of international organizations was taken into account. Japan was chosen as a country that has a positive experience of IMF money attraction in opposite to Russia<sup>8</sup>.

Despite the fact that hierarchy and sequence of a statement of base abstracts of law related to foreign investment differ from country to country the common moments can be found. They include:

1. Interpretation of concept of "foreign investment"
2. The services of control and regulation of foreign investment.
3. The procedures of an access on the national markets and necessary forms of report.
4. Opportunities to get a credit in national banks and a list of payments that might be interacted in foreign currency.
5. A list of privileges given to the foreign investors.
6. The criteria used for approval of those or others investment projects.
7. Forms, legal and organizational, in which the foreign investment could be made.

<sup>3</sup>For comparability of the analysis of the enterprise of the various countries are compared on a volume of output, size of profit and number of the occupied.

<sup>4</sup>Laws and Regulations. Amman Stock Exchange.—www.ase.com.jo.

<sup>5</sup>Investment Laws and Trade's Regulation. Federation of the Syrian Chambers of the Commerce.—www.fedcommsyr.org.

<sup>6</sup>Oman. Chamber of the Commerce and Industry.—www.arabdatanet.com.

<sup>7</sup>Israel: Country Commercial Guide FY. 1999.—www.israel.us.ittn.org.

<sup>8</sup>Japan is not an exception because from the point of view of international market of capitals it is certainly not the 'small' economy

8. The branches and territories where the investment is permitted and not.
9. Priority directions of investment.
10. Application of other international investment rules with one or another grade of fullness.

## 2. CHECK THE FDI'S ROLE FOR SOME SMALL COUNTRIES

The concept "international investment" doesn't differ practically in legislations of considered countries and correlates with an accepted meaning in international practice in majority of parameters. The investment legislation supposes the same structures of control and regulation of international investment. The special governmental organizations are created in many countries that regulate a participation of foreign investors in a country economy. In Jordan and Syria it is a High Council of investment attraction. In Oman – the international investment committee, in Israel – the investment center. Besides in the countries of Middle East there are some other governmental organizations and agencies that are in response for those or other spheres of international investment. They could differ in the level of submission to the head of a state, the number of members which is determined by the different state priorities. The Committee of foreign direct investment was created in Japan in 1992. The council of investment with a prime-minister ahead was created in 1994 as the assistance for foreign investment was important for the country economy.

Organizational and legal forms in which the foreign investment can be made differ from country to country. There are no standard decisions here. Each country in dependence on the developed national practice establishes those or other forms. Nevertheless we can speak about the existence of common approach in access of foreign investors to the national markets of a country. These are special conditions for investors from friendly countries (according to territorial or national criterion); restrictions on the size of a share of foreign participator in a company (100% of participation is restricted, the only joint factories are permitted); the requirement of providing the definite share of foreign participator in company profits (in any circumstances this share could not be less than 35%) the only Israel legislation permits the creation of a factories with a 100% of foreign participation<sup>9</sup>.

Let's do the empirical test about correlation between national legislation and international rules.

*The right of entry.* In Japan the establishment of foreigners access zones is permitted; the requirements of the sum of insurance payments are decreased, the

special notice about the supposed investment is not required. In agriculture, forestry, oil and a mining industry, manufacture of furriers and leather products, at the enterprises of air and sea transport for foreigners the special mode of investment as they are considered as the branches providing economic safety of the state is applied.

The legislation of Venezuela provides the most favorable mode for foreign investors and to-tally corresponds the international norms. There is need to pay a special attention to the fact that losses from military conflicts, crisis or acts of nature are covered by restitutions, indemnification payments etc. on the same favorable conditions as for national investors.

In Norway in the branches monopolized by the state (post, railroad, the retail selling of alcohol) both national and private foreign investment are forbidden. The foreign investment in the energy industry is restricted by the 20% of assets. The participation of foreign investment in manufacture, financial sectors and mass-media are under the control of a state with a help of concessions. Besides any private company could not have more than one third share of national radio or Television Company. If the share of foreign property in a company is more than third the concession agreement does not permit the participation of a company in other deals. It is proved by protection of the national business interests and the necessity of keeping the work-places. The Norway stimulates the inflow of investment in the northern part of a country through the application of decreased profit tax.

The legislation of Jordan restricts the foreign participation in air transport, branch of contract building, trade and branch of services, in bank, financial, insurance, mining, agriculture and tele-communication branches of economy. On the other side the list of priority branches and directions of investment is formed and if the investment is made in that directions the privileges and grants or even total tax free are provided.

In the legislation of Syria the classification of investment projects is made not only according to presence/ absence of foreign investment but also according to the form of property. For each of forms the own procedure of registration and conduction of an account is provided. To get the privileges established by that law the directions of priority investment and the minimum of deposits in basic money of a project are determined (10 million of Syrian pounds is equal to \$516,8 million by the rate of April 2002). The rules of joint manufactures creation is determined separately. For license reception an investor (resident or not resident) should buy or rent a ground and real estate in Syria that might become a serious obstacle in expansion of existing projects and investment into the new projects.

<sup>9</sup>Israel: Country Commercial Guide FY1999.–[www.israel.us.ittn.org](http://www.israel.us.ittn.org).

In Oman there is a forbid on the foreign investment into the sphere of engineering, architecture, jurisprudence and accounts department. The foreign consulting companies working in the spheres mentioned above and others established earlier than 1996 have to find the Oman partners in concrete definite for each company term. For creating a joint enterprise, opening the office or buying the action of Oman's companies the foreign investor should get the license from ministry of trade and industry and also other ministries in dependence on the branch of business (the ministry of regional municipality and environment, the ministry of work). Especially serious requirements are applied to the manufactures where the share of foreign investors in the capital is more than 70% or the total capital of a manufacture is \$52 thousands or more. The minister of trade and industry makes a decision whether to give a license for manufacture or not.

The Israel economy forbids the foreign investment in the branches of defense industry and branches of economy providing the national security. For foreign investment in the branch of insurance and bank sphere there should be the governmental license.

The analysis of a first rule – the “right of entry” – leads to the conclusion that national legislation of considered countries restricts the activity of foreign investors and in fact the necessity of foreign investment attraction in economy is very often the declaration only. The discrimination has a place basically not in the media foreign investors but there are differences in conditions of investment for residents and not residents.

*Fare and equitable treatment.* Justified and non-discrimination regime. According to legislation of Norway a national regime have been provided for all foreign investors since 1994 including territories and branches which were forbidden or restricted. However there some instructions that provide more favorable conditions for the investors from Scandinavian and EEA countries (The acceptance over a freedom of trade between Norway, Iceland, Liechtenstein, and EU). Oil and gas branches are the exceptions from those instructions because three national companies of Norway have a privilege regime.

The legislation of Jordan guarantees the equal rights for both residents and non-residents.

The legislation of Syria also doesn't accent the attention on the differences between foreign and national investors or between different foreign investors so we can consider that the rights of foreign investor are equal to the rights of national investor however there are some restrictions on the in/out and converting the currency. 25% of earned foreign currency should be sold to the commercial bank of Syria by the official exchange rate. Converting of a salary to a foreign currency while the realization of a project is restricted by 50%, the rest part could be converted only when the project is completed.

Temporal restrictions also connect the transfer of pure profit: the transfer could be made only in 5 years after the investment project starts. Therefore a legislation of Syria acts like a nipple: lets in easily but sharply controls the investment outflow from the country at least during the time of investment project realization.

The investment legislation of Oman uses different approaches in fiscal policy for foreign and national investors. Particularly a manufactures where a foreign participation is more than 70% the corporate profit is taxed by a maximum rate of 30%. At the same time a rate for national companies is 12%. The legislation of that country does not provide restrictions of additional requirements to foreign investors over repatriating of profits, converting and transferring of salary and other payments. The capital flows into and out of Oman are so liberalized that there is need to contract the money-laundering.

In Israel receive of privilege or national regime of investment connected with a receive of a status of approved manufacture. The size of received privileges and grants depends on the branch where the investment is directed, the type of investor, the price of a project and its geographical location. The “Zones of national priorities” according to geographical criteria are determined that also have a different level of privileges. The size of grant depends on the volume of investment in the basic capital of manufacture. Usually the government of Israel requires at least 30% of project to be invested by personal capital of investors. There are some temporal restrictions for granted projects: 25% of work according to the project should be done during the first year and 25% of work should be completed during 3 years after the receiving of an “improved” manufacture status.

*The contract terminated.* The Norway cancelled any control over the money transfers of foreigners in the beginning of 90s of XX century. There have not been noticed any cases of non-approved confiscations since.

According to Jordan legislation if the property of investment project is expropriated the obligatory and full indemnification payment is paid in convertible currency.

The legislations of Syria provides that the investment projects should not be confiscated, expropriated or restricted to dispose with their investment property and profits if the public interest is broken and the honest indemnification payment is not paid.

The basic share of Oman economy belongs to the state. In the bounds of held program of privatization the government provides the guaranty of fights of foreign investors in the case of expropriation or nationalization. However the law of 1974 which is about foreign business and investment does not provide the indemnification payment in the case of contract stop.

*The dispute of settlement.* According to Venezuela legislation the dispute could only settled according to Washington international convention.



In Jordan a dispute between foreign investor and authorities is settled by the acceptance of sides. If such an acceptance is not reached during 6 month each side has a right to start a judicial process and apply to "International center of investment dispute settlement". It means that in the internal court of Jordan the consideration of cases is not supposed.

In Syria the settlement of investment disputes located under the Syrian jurisdiction. The 6 month term for reaching an acceptance is provided also and any side has a right to apply to arbitrage court of a country or Arabian investment court.

In the case of disputes occurrence with a participation of foreign investor the settlement is realized on the territory of Oman sultana. This is a competence of Commercial court that settles disputes on tax and work legislation. It is accepted that the decisions of Commercial court could not cancel the decisions of international arbitrage if such is provided by contract. However a Sultana requires all foreign companies to follow these courts solves. There is need to notice that in the case if a foreign investor starts an affair versus the state the Commercial court has a right to consider this affair but the decision made by the court does not have an obligatory judicial power. The decision of the Commercial court is accepted as a final in the commercial disputes which sum is not more than \$26 thousands. The consideration of affairs where the considered object is a greater sum is in competence of an Appellation court which decision is final also. The reconsideration of an affair is possible if new documents or above the law actions (falsification, false witness) of one side are found. The less difficult questions of a dispute the sides could use services of arbitrage

committee of trade and industry palace.

In case of occurrence of dispute which participants is the foreign investor and the government of Israel, business is considered by the International arbitration on investment disputes between foreign investors and the state. Its decision admits the government obligatory. All payments under the decision of disputes are carried out in national currency.

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## CONCLUSION

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On the basis of the analysis of activity of the small number of countries we can't make conclusions about efficiency of application of rules for all countries of the world. Nevertheless, carried out research allows to testify, that the governments of the majority of the countries concern foreign investments as "compelled", that they try to direct activity of foreign investors on development of own economy. Performance of rules sometimes appears insufficient.

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